

STATEMENT OF
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HUD CONTRACTING: VULNERABILITIES AND PROPOSED SOLUTIONS

Chairman Shays and Members of the Subcommittee, I appreciate the opportunity to testify, along with Edward Momorella, about HUD contracting issues. Mr. Momorella, the OIG's District Inspector General for Audit in Philadelphia, directed the nationwide audit that resulted in the Office of Inspector General's (OIG's) September 30, 1997 report titled "HUD Contracting."

Our testimony today will review i) the principal findings of the OIG's September 30, 1997 audit report; ii) HUD's reactions to the audit report; iii) current efforts to improve HUD contracting, as the OIG understands them; and iv) the importance of efficient and effective contracting to HUD's 2020 Management Reform Plan.

The OIG's September 30, 1997 Audit Report on HUD Contracting

By letter dated November 14, 1996, Senator Bond, Chairman of the Subcommittee on VA/HUD Appropriations, and Senator Faircloth, Chairman of the Subcommittee on HUD Oversight and Structure, asked the OIG to comprehensively review HUD's use of its contracting authority. Their request was based on concern, as HUD downsizes, about the risks associated with HUD's reliance on contracting its responsibilities.

In response to the Senators' request, between February 1997 and June 1997 Mr. Momorella directed a team of 26 auditors in reviewing HUD contract activity from 1992 through 1996. During this period, HUD awarded about 9,600 contracts worth over \$3.2 billion. The OIG team examined in detail 63 contracts worth \$1.5 billion held by 30 contractors. In the process of the audit, the team interviewed more than 225 persons, including HUD managers, Contract Specialists, Government Technical Representatives and Monitors, contractors and unsuccessful bidders.

Our selection of the contractors and contracts for detailed review was judgmental--we wanted to provide broad coverage of HUD programs and services and to focus on areas of greatest vulnerability. This targeted focus notwithstanding, it is significant that the auditors found problems in virtually every contract they reviewed.

The September 30, 1997 audit report identifies seven major categories of problems in HUD contracting:

1. Need Determination, Planning, and Periodic Assessments.
A lack of adequate planning, needs assessment, good initial estimates, monitoring, and control of performance and cost expenditures on several multimillion dollar contracts has made HUD vulnerable to waste and abuse.

While initial need determinations were documented for most contracts, OIG auditors found little in the way of periodic reevaluations to assure the contract was still beneficial to the Department and worth the cost. Many contracts were extended longer than anticipated and more costly than originally estimated. In some instances, products or studies took so long to complete that the results were no longer useful to HUD because of changing program priorities.

2. Cost Consciousness. HUD often contracted for a desired outcome without specifically knowing what tasks to request to achieve the outcome. While this may be a time saving process to award the contract, it often is the most costly, as HUD was unable to prepare good cost estimates on the tasks needed to accomplish the end product. As a result, the contractors had a clear advantage, as HUD was not in a position to reject costly modifications or time extensions, at the risk of having to start all over again.

By paying closer attention to negotiating contract terms, contract types, and overhead rates, HUD could save millions of dollars, especially in the area of information technology and consulting contracts. Management's contracting environment needs to change to seek ways to emphasize cost consciousness and assure the best value for dollars spent. Because HUD managers did not have the staff to complete the product or service in house, the question of "What will it cost?" was often not seen as an issue.

Current contract costs could be significantly reduced by providing better government estimates and allowing more competition. Indefinite Quantity Contracts (IQCs) gave HUD the flexibility of quicker and easier procurement, but often cost more because no competition was required for individual task orders. Without well defined task orders, HUD often had no idea what the final cost would be for these services.

3. Contract Oversight and Monitoring. OIG auditors found contract monitoring very lax throughout HUD programs. In some cases, HUD had contractors monitoring contractors. Many Government Technical Representatives (GTRs) and Monitors (GTMS) had a poor understanding of their respective roles and responsibilities. Indeed, training was not a prerequisite to being assigned as a GTR or GTM.

In several instances, the current GTRs were not involved in the original award or even knowledgeable about the purpose or usefulness of the contracts. Where top level managers were assigned as GTRs, often they were too busy addressing other organizational and program crises to pay much attention to contract management. Where mid and lower level staff were assigned as GTRs and GTMs, most regarded their contracting roles as ancillary to their positions--something to do only if they had the time. In fact, contract management was not one of the performance elements they were rated on.

4. Contracting for Prohibited Services. OIG auditors found several instances where HUD has contracted for services that appear to be prohibited under the Federal Acquisition Regulations and HUD's Procurement Policies and Procedures. These prohibited services included personal services contracts, advisory and assistance services contracts to aid legislative initiatives, and contracts to perform inherently governmental functions.
5. Data and Financial Systems. Until early 1997, the Office of Procurement and Contracts (OPC) had maintained a data system to keep track of contracts awarded at headquarters; field offices had maintained separate systems to keep track of their contract awards. OIG auditors found numerous data errors and omissions in the OPC system, and concluded that it was not reliable for comprehensive contract management.

In early 1997, HUD combined the OPC and field office systems into one system, the HUD Procurement System (HPS). While this goes a long way in improving OPC coordination and standardization between Headquarters and the field, HPS still lacked integration with the financial systems in HUD's Office of Finance and Accounting. This integration is essential so that GTRs can readily determine exactly what has been paid or drawn per contract per task order.

6. Contract Close-out Procedures. Approximately 50

percent of the contracts awarded by HUD are cost plus contracts. Under this type of contract, one of the critical steps for the Department is the final or close-out audit. This is the Department's assurance that the contractor charges only costs directly related to the contract and that applicable overhead rates and other fees are appropriate. OIG auditors found a high number of cost plus contracts that had been completed, for which close-out audits had not been performed or requested.

7. Interagency Agreements. The Department paid other Federal Agencies over \$263 million for services provided under numerous interagency agreements. In some instances, these agreements go back many years, and current GTRs could not explain certain provisions of the agreements, or what cost methodology was used to determine reimbursable amounts.

The September 30, 1997 audit report illustrates each of these problems in terms of specific HUD contracts.

While the OIG audit was in process, the Department contracted with the National Academy of Public Administration (NAPA) for a review of contracting by the Federal Housing Administration (FHA). The initial NAPA review, issued in May of 1997, concluded that FHA's contracting system neither responded effectively to Department needs nor adequately ensured accountability. The Congress then directed HUD to contract with NAPA for, among other things, a top-to-bottom redesign of the HUD procurement system.

The first deliverable under the expanded NAPA contract was a February 1998 Interim Report, which focuses on improvements needed in FHA/Office of Housing contracting and makes recommendations on how to bring about those improvements. NAPA's Interim Report reiterates the findings of the OIG's September 30, 1997 Audit Report, as well as the findings of NAPA's initial review of FHA contracting. It concludes that:

- Housing/FHA cannot accomplish its critical work with the current [contracting] system.
- "Fixing" specific steps in [the contracting] process will not be sufficient to address [the] complex, interdependent challenges of: ensuring accountability and integrity; effective risk management; and effective contract administration.
- Housing/FHA is unlikely to implement these [NAPA's] recommendations without a clear mandate and

accountability.

HUD's Reactions to the OIG Audit Report

The audit report was issued in draft to HUD's former Deputy Secretary on August 7, 1997. The former Deputy Secretary responded on September 8, 1997 with a two-part message. First, the former Deputy Secretary said that the OIG draft report validated the conclusions reached by NAPA in its initial review of FHA contracting, and the OIG recommendations would be provided to NAPA for consideration as part of the contract system redesign. Second, the former Deputy Secretary said that the OIG draft report was "flawed in its methodology, [contained] factual inaccuracies, and [was] unbalanced in its characterization of specific contract actions," and therefore inconsistent with Generally Accepted Government Auditing Standards. The Deputy Secretary's response is Appendix A of our September 30, 1997 audit report.

When the audit report was issued in final on September 30, 1997, the OIG requested--within 60 days--a status report on each recommendation in the report, indicating i) the corrective action taken; ii) any proposed corrective action and the date to be completed; or iii) why action is not considered necessary.

The Department's response came 160 days later, on March 10, 1998. The response promised immediate institution of the following procurement reforms: establishment of a Chief Procurement Official (CPO); mandatory training and certification for GTRs/GTMs; inclusion of contracting rating elements in the performance plans for GTRs/GTMs; Office of General Counsel participation in certain procurements; and improvements in HPS. The response also reported that the Office of Procurement and Contracting had made substantial progress in requesting overdue close-out audits, and had also taken measures to prevent future backlogs in this area.

Notably, the Department's response disagreed with the OIG's assessment that certain HUD contracts were prohibited under the Federal Acquisition Regulations, but failed to provide any basis for this disagreement. Further, despite the delay in responding to the audit, the Department reported no action on the OIG's recommendation that the Department i) review problems identified by the OIG with regard to specific contracts and interagency agreements; then ii) determine what steps are necessary to protect the Department's interest; and iii) where necessary, either amend or terminate contracts/agreements not providing a necessary service or cost efficient results. The response was simply that the Chief Procurement Officer, when hired, would be tasked with reviewing these matters.

In summary, the Department has committed itself to prospective corrective actions, but has not embraced the opportunity to right past wrongs and exact accountability for them.

Current Efforts to Improve HUD Contracting

Most importantly, HUD has hired Steve Carberry, a highly experienced contracting professional, as Chief Procurement Officer. Today, you will undoubtedly hear about Mr. Carberry's plans for/progress in establishing a Contract Management Review Board; establishing a cadre of full-time GTRs and GTMs; instituting GTR/GTM training; placing procurement rating elements in GTR/GTM performance plans; and establishing meaningful performance measures for a reformed HUD procurement system. This is all good news.

The not-so-good news is that there has been no official definition of Mr. Carberry's authorities, responsibilities, or placement in the organization. This is a critically important matter: reforming HUD contracting is going to require, among other things, a change in the HUD culture, and the CPO is not going to be in a position to force that change if he is understood to be in a subordinate position vis a vis the program Assistant Secretaries.

Similarly, Mr. Carberry briefed the HUD Management Committee this week on his plans and progress, but we have seen no written definition of these efforts. This is not just a matter of being bureaucratic: the OIG would like to see the proposals laid out so that we could offer our advice and counsel up-front, rather than our criticism after the fact.

In the same vein, we applaud the Department for meeting its obligation to appoint a Chief Information Officer (CIO). This position is critically important to the reform of HUD contracting, since information technology contracts represent the highest dollar amount of contracting in HUD. Again, Gloria Parker, the new CIO, has superb credentials for this position. But, as yet, there has been no official definition of Ms. Parker's authorities, responsibilities, or placement in the organization.

The Importance of Efficient and Effective Contracting to HUD's 2020 Management Reform

As noted above, HUD has historically done a substantial amount of contracting: 9,600 contracts worth over \$3.2 billion were awarded from 1992 through 1996. Under the Secretary's 2020 Management Reform plan, HUD staff has been downsized while ambitious new performance goals have been set throughout the Department. Attaining the new performance goals will be heavily

dependent on additional procurements for services such as single family property disposition, physical inspections of multifamily and public housing, Section 8 contract administration, and definition of a resource estimation system for HUD. The OIG estimates that these additional contracts could easily involve more than a billion dollars a year.

It is unfortunate that HUD staff was downsized and plans were developed for additional contracting without a cost benefit analysis. At this point, however, that is water under the bridge. The key point is that an efficient and effective procurement and contracting system is absolutely critical to HUD's meeting its HUD 2020 Management Reform goals. To illustrate this point:

- A major objective of HUD 2020 is to integrate HUD's financial systems. In the information technology area, HUD's reliance on contractors is virtually total.
- Another major objective of HUD 2020 is to ensure that the multifamily and public housing programs in fact provide decent, safe, and sanitary housing. This objective is heavily dependent on a new HUD physical inspection program to be carried out by contractors.
- In the single family area, HUD 2020 aims to improve the property disposition function by contracting it out. Single family staffing has already been reduced accordingly.
- HUD has contracted with NAPA to devise a resource estimation system for the Department. This is intended to correct HUD's material weakness in the area of staffing and administrative resource management.
- HUD 2020 further intends to better assure the accuracy of project-based Section 8 payments by using contractors rather than HUD staff to administer this payment function.

Mr. Chairman and Members of the Subcommittee, that concludes our testimony. We thank you for holding this important hearing, and giving us the opportunity to testify.